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SHIFTING THE WAR BURDEN UPON THE FUTURE

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Congress has already appropriated nearly nineteen billion dollars for expenditures of the current fiscal year which ends June 30 next. In addition, it has authorized contracts of over two and a half billions for which it has not yet made appropriations. Part, though not all, of the money will be needed on these contracts this year, so that our total expenditures in round numbers will be twenty or twenty-one billions if no more are authorized. Our federal revenue laws have been revised recently so as to raise about three and three-fourths billions through taxes. If they are not further revised, this will leave sixteen or seventeen billions to be raised through loans, or a ratio of loans to taxes of about four and one-half to one. We have already subscribed about six billions in loans so we still have to secure about ten or eleven billions in loans and nearly all of the taxes. This means that about fourteen billions, or two-thirds of the total amount necessary, are yet to be secured after payment of subscriptions to the current bond issue.

It is extremely difficult for us to appreciate what it means to raise twenty-one billion dollars in a single year. This is over twenty-five times our ordinary federal expenditures prior to the war, it is twenty times our national debt of a year ago, it is over seven times our national debt at the end of the Civil War, and it is over four times the combined cost of all of our five wars beginning with the Revolution. Furthermore, it is more than all of the Entente Allies spent in either the first or second year of the war, it is four-fifths as much as Great Britain, the largest spender, has used in three entire years, and it is two-thirds of the combined expenditures of all the central powers in the same three-year period.

But these stupendous figures do not become real to us unless we consider them in terms of the sacrifice which they will mean. The most accurate estimate of the national income of this country puts it at about thirty billions in 1910. The most recent estimates are based upon this, and, after allowing for the increase in prices and

for increased production due to more general employment, greater population, speeding up, etc., they put the present national income at forty-five to fifty billions. Our present plans call for a diversion of over two-fifths of this amount to war purposes. To put it in another way, the twenty-one billions mean an average of \$200 for every man, woman and child, or \$1,000 for every family of five in the United States. Reduced to these terms, we can begin to visualize what a tremendous burden this involves, though few of us can comprehend that it is really to fall upon ourselves.

Although many have not thought of the burden in very concrete terms, some others have realized that twenty billions is an enormous sum to raise and that taxes twenty-five times as heavy as heretofore would be very grievous; hence many plans have been suggested to obviate the use of such taxes and to avoid or lighten the burden through borrowing. There are few fallacies so plausible and yet so harmful and general throughout the land as those involved in the idea that we can shift the larger part of the burden of this war to the future by substituting loans for taxes. One reason that this idea is so harmful is that it contains all the evils of a half truth; another and most important reason is that we are confused with money and monetary terms so that we do not see clearly the real things for which money stands.

When we stop to think we know that it is not twenty-one billions of dollars which our government wants ultimately, but twenty-one billion dollars worth of commodities and services. Our national income does not consist of forty-five or fifty billions of dollars of gold, silver and paper, but of that many dollars worth of wheat, lumber, minerals, clothing, automobiles, etc. There are less than five billions of actual gold, silver and paper dollars in existence in the United States. These dollars are the counters in terms of which the real things are measured and by means of which they are exchanged more easily. For our present purposes to have gold, or silver, or paper is not to have anything of value in itself, but merely to have a claim upon real things for which it can be exchanged. It is obvious that our government needs money in order that it may exchange it for men and commodities, for it is with these that it must fight the German military forces. It is obvious, also, that it must have these men and commodities now. Munitions of 1930 and men not yet born cannot be hurled against the enemy's lines. The burden of

furnishing all of these things must be assumed now, it cannot be put off till the future.

If we could borrow from other nations, we might fight the war with what they loaned to us and we ourselves go ahead consuming what we produce, as we have been doing before the war. In that case, we could shift the paying of them, that is, the burden of the war, to the future. But there are no other nations who can lend to us at this time; we ourselves must raise an army, equip it and keep it supplied. Not only must all of this be done at home, but in addition, we must help to feed and equip our allies. None of this can be left to the future.

Of course the next generation will be injured because of this war. Billions of dollars worth of labor and food and steel and other materials that are now absolutely destroyed in war are diverted from the construction of railroads, irrigation systems, manufacturing plants, improved roads, houses, all of which might have aided our descendants and made their lives fuller and happier. If a man's property is destroyed his children receive an impaired heritage, both he and they suffer. Our descendants must suffer in this fashion because much of their patrimony is being destroyed. But we cannot, as a nation, postpone our burden if we would, nor can the future help us. Then why delude ourselves with thinking that it can?

But while it is impossible for this nation to shift part of the burden to the future, it is possible for certain individuals and classes to shift parts of their shares on to other individuals or classes, both now and in the future. This is true whether all of the means to prosecute the war are secured through loans or taxes, or both. Let us consider the two means of taxes and loans, respectively. Realizing that everything needed must be secured now, everyone will concede that each individual should pay his just share. This will mean a much greater part of large incomes than of small ones, but we shall not here go into details of exactly what constitutes a just share. We merely assume that each should pay his just share when what is just has been determined.

We may assume first that each individual pays his share in the form of taxes. These taxes might be paid in money or in kind. In either case, what the payer gives up and what the government gets ultimately is services and commodities. For this payment, the government gives the payer a tax receipt. Suppose on the other

hand that each individual gives up to the government his just share in the form of a loan. This is exactly the same amount as we supposed in the first case that he gave up in taxes. In this case, as in the other, it may be in money or in kind, and, similarly as in that case, he really gives up and the government gets services and commodities. The only difference in the two cases is that in the first one he has a tax receipt and in the second he has a government bond, a promise that he shall be paid back with interest.

But let us consider the paying back process. If the future taxes are levied justly, each one (or his heirs) will be taxed just enough to pay his own bond and whatever interest it draws. That is, he merely transfers money from one pocket to another and his bond is paid. When he lent to the government and thought he was better off than if he had paid taxes, he deluded himself.

It is obvious that if anyone pays less than his just share, someone else must pay more. But when a war comes unexpectedly it may find many individuals unprepared to pay their just shares of a new and large burden. It may be best all around to permit some to assume the burden of others temporarily, either wholly or in part. This may be done whether the government supplies its needs through loans or through taxes. Because this is so apparent in the case of government loans, we shall consider only the case of taxes. Assume that the government is to secure everything through taxes. Assume two men of equal ability to pay taxes. At the time the war burden comes A has a large shoe plant turning out thousands of pairs daily. B has a smaller plant, but he is building a large additional one to construct which he is borrowing, besides turning into it all the proceeds from his existing plant. Let us assume that neither has other liabilities or assets. It is obvious that A can use his proceeds above living expenses, either to pay taxes or to buy bonds. The amount thus available for government use is probably greater than his share of the government requirements, at least, he probably can make it greater by reducing his ordinary consumption of luxuries and near luxuries. But it is not so convenient for B to pay taxes. The only way he can do so is to give up his new plant which would involve great loss, or to borrow more. He ought to be able to borrow and A is in a position to lend to him. That is, A advances B's taxes, and later, when B's larger plant is turning out its full quota and his debt for construction is paid off, he concludes the transaction by paying

his debt to A. In other words, for the time being, B shifted his tax burden to A and later B repaid A with interest and each profited by the transaction.

In this last assumption, the government secured everything through taxation, nothing through loans. But this same thing might have been accomplished through government loans. Assume again A and B as in the last case. The government offers a bond issue. A is in a position to buy bonds, but B is not. In buying more than his share of bonds, A is really lending, through government agency, to B, who is not now in a position to buy his share. Now observe the process of paying off these bonds. Though A and B were equally able when the war came on, B is now more able to pay taxes because A has lent the proceeds of his plant while B has not only loaned but has put his proceeds into a bigger plant so that he now has more property and a greater output than A. Both A and B must pay taxes to redeem the bonds. If the burden is distributed equitably on the basis of our former assumption, A's taxes will be enough to pay himself, not all the government owes him, but just the amount which would have been his just share of taxes plus interest on the same, if he had paid taxes in the first place instead of buying bonds. B's taxes will pay the rest due A and they will be the exact amount which B would have paid in taxes plus interest, had he paid taxes in the first place instead of letting A buy bonds equal to the share of both. In so far as the government can make easier advantageous credit transactions by itself assuming the borrowing agency instead of leaving the transactions to be arranged between individuals, there is a further net gain. This is the real essential economic justification of government loans.

We shall take up later some of the offsetting losses occasioned by the borrowing plan. But before we go further, we should note again that whether the government supplies its needs through taxes and thus necessitates private borrowing, or whether the government itself does the borrowing, the shifting of the burden is not from the present to the future so far as the nation as a whole is concerned. All the shifting now and in the future is between individuals. If there were no offsetting losses the total net burden would probably be a little less in the present because of the government loans but the national burden of the future would hardly be affected one way

or the other. It would be merely a matter between individuals; what was given up in taxes by certain persons would be received by part of themselves in payment of bonds and interest. It is conceivable that this redistribution of income might be either advantageous or disadvantageous from a national standpoint.

This point may be made more vivid if we consider the case of Germany who has been unable to borrow much from outside her own borders. Because of this fact many said at the beginning that Germany could not last long. But she has demonstrated that she is a powerful enemy with an unconquerable fighting machine just so long as she can provide men and materials. Having mere gold and silver is a secondary matter, but having the necessities of war when needed rather than in the future has been her chief strength. True, she has floated huge internal loans but that has not postponed the national burden of carrying on the war, it has merely been a shift between various citizens of the empire as becomes obvious if we consider what would happen if the internal debt were repudiated later. In such a case the taxpayers would retain the money which would otherwise be transferred from them to those who owned bonds. In so far as the taxpayers and bondholders are identical, the transfer of money would be first to the government and then back to the individual. Of course, the same reasoning applies to the United States.

The advantages of accommodation which government loans permit are very great in the beginning of a war when readjustments are being made and while a new tax system is being made productive as Professor Adams¹ points out. Later they lose much of this advantage and they involve certain important disadvantages as compared with taxes. One of the most important of these disadvantages is that the burden of taxation is apt to be distributed more equitably if the taxes are levied during the war than if after its close. The well-to-do classes have practically always controlled legislation directly or indirectly and they are much more likely to be willing to assume their just burdens during the war while the spirit of patriotism is almost universal and while others are giving their lives to the country. After the war closes they are much more apt to resort to indirect taxes which fall upon people in proportion to what they consume rather than in proportion to their ability to pay.

¹See pages 28-30.

In this connection I should call attention to Professor Seligman's² statement that the experience of the Civil War showed that the reverse is the case. It is true, as he stated, that many of the excise taxes were repealed before the income tax which fell more heavily upon the well-to-do. But the significant fact which he did not mention is that the high tariff duties, which during the war were merely compensatory, were retained for half a century after the war and during all of that time formed the bulwark of federal revenues as well as a source of privilege to the industrial entrepreneurs. Few warnings of the Civil War are more important in the present case than that suggested by this experience. In the violent readjustments which the close of the war will necessitate, we are almost sure to have a widespread demand for protectionism and the revenue needs of the government are apt to be used as a strong argument for this form of subsidy to the few at the expense of the many. Hence, there is a triple reason for high taxes during the war: first, the patriotic call which will mean more equitable distribution than later; second, high prices during the war which cut down the standard of living of the masses but bring greater profits to the employers of labor and the large scale producers and sellers of war necessities, thus enabling them to pay high taxes; third, the demoralization of readjustment following the war which will bring an immense decline in profits and ability to pay excess profits and other taxes and which will at the same time cause great numbers of soldiers, munition makers and others to be taken off of the government payrolls and put upon those of readjusted private industries.

A still further and indeed the most important advantage of taxes over loans is that, if levied properly, they are much more likely to cause everybody to economize in accordance with his ability to do so. If one has to pay \$100 or \$1,000 in taxes, he is much more apt to economize immediately than if he lends that much to the government thinking that he has an investment which will not only bring interest but which will be paid back later. He forgets, or never realizes, that he may have to repay himself later, and hence is inclined to save less than if he had made a gift or paid a tax to the government. Furthermore, he knows that if he has unexpected financial needs in the future he can sell his bond and get his money back, or that he can borrow on it at the bank, so there is not the

² See page 72.

necessity for him to economize as in the case of taxes. We shall attempt to show a little later the extreme necessity of widespread and stringent economy.

All economists, including the few who advocate a large proportion of loans as compared with taxes, as well as the many who advocate the reverse proportion, agree that the borrowing of money from the banks to buy bonds, or the borrowing upon bonds as collateral, or the purchase of bonds by the banks is certain to cause inflation. Furthermore, all agree that this inflation, by causing a rapid rise in prices, injures very seriously nearly all wage-earners, salaried employes and all receivers of relatively fixed incomes, but benefits those who pay these wages and other relatively fixed incomes, and especially those who have large quantities of commodities to sell. In other words, inflation means a redistribution of income and property, mostly in favor of the active business class and to the misfortune of the large laboring class. But the details of inflation, how it is brought about and how it works, I shall leave for others to discuss. Suffice it to say that the evils are extremely great as our own experience in the Civil and Revolutionary Wars and as experience in scores of other cases has abundantly proved.

The idea that we can put off a large part of the war burden till the future and the policy of huge loans and inadequate taxes which it encourages are largely responsible for our failure to economize now as we should. As already mentioned heavy taxes would immediately bring home to us the necessity of economy. But as it is, many still continue to preach "business as usual" and many others think the war can be financed by some sort of financial legerdemain. They do not begin to realize the extent of the sacrifice which it means.

Let us recall that after allowing for speeding up, increased population, more general employment, higher prices, etc., the best estimates of our national income place it at forty-five to fifty billion dollars, and that Congress has authorized expenditures of two-fifths of this income for war purposes this year. Let us recall, too, that this income and these expenditures are not dollars but that they are real commodities and services. The government cannot by any financial hocus-pocus get twenty billions worth of commodities and services unless we give up that amount and live on the remainder. If business continues as usual, it means that we demand the same

necessaries and luxuries as before, that the same men and farms and manufacturing plants are necessary to produce these goods as before and that the government can secure nobody to fight in its armies or to make ships, munitions and other extraordinary things needed to carry on a war. It is possible to carry on a huge extra undertaking like the war only by diverting a large part of our energies from the usual channels. Everyone who does not save, who still demands the same goods as formerly, prevents the labor which produces what he consumes from being diverted to government use. Those who give up luxuries and near luxuries permit the labor and materials and plant used in their production to be diverted to making necessities of life and munitions and other commodities needed to supply the military forces. We have already shown that this diversion must take place now, to put it off till the future means to lose the war. If any person does not do his share of saving, someone else must save more. But laboring under the delusion that this burden may be shifted in large part to the future, very few of us have begun to economize to the extent of two-fifths of our income, which is the average amount that must be saved to carry out present plans.

It is estimated that heretofore we have been saving five or six billion dollars annually and with it constructing new capital in the form of additional railroad, irrigation, manufacturing and other plant. If all of this construction could be and were stopped and the labor and commodities which have hitherto gone into it were turned to direct war purposes, we would have to reduce our ordinary consumption by only fifteen billion instead of by twenty or twenty-one billion, that is, by only a third instead of by two-fifths.

But it will be said that not everyone can reduce his consumption by a third. This is true of the masses with small incomes, but it is not true as many seem to think, that the rich can bear all or nearly all of the burden of twenty billions a year. Their total income does not amount to that sum. Dr. E. Dana Durand, than whom there is no more competent authority in the United States, has calculated that only one-tenth of the entire national income is received by those having incomes in excess of \$25,000. In order to secure two-fifths of the total national income it would be necessary to take 100 per cent of all of the family incomes in excess of \$1,500. Even if allowances are made for recent changes in American incomes, it is apparent that the rich alone cannot finance the war. While it

is true that they can make much the largest contributions per family and even in proportion to their total incomes, still it is necessary that all classes shall economize.

Besides the misconceptions mentioned above, there are many others current throughout the country. Among them we shall take time to mention only a few of the most popular and plausible ones. We are told upon all hands that, of the twenty-one billions, seven billions are not our own expense but are for loans to the allies. So far as the war period is concerned, these loans are to all intents and purposes our own expense. Like ourselves, the allies want and must have commodities, not gold and silver, and we can furnish these to them only by doing without them ourselves.

In connection with our loans to the allies there is another common fallacy in the implied advantages which we are to receive because all of these loans will be spent in this country. It is true that this will mean more work and a greater demand for our commodities and this is probably a good reason why those who are thus specially benefited should subscribe more liberally for bonds. But for the nation as a whole this is not an advantage but a distinct disadvantage. We do not at the present need more work, rather we need more help to perform the enormous tasks before us. The pity is that the allies and ourselves cannot spend this money to advantage in other countries so that we might have that much additional aid in overcoming the common enemy.

Another misconception is common among those who urge the withdrawal of savings bank deposits to buy bonds as well as among those who urge insurance and other investing companies to accept government bonds in payment of premiums. To withdraw savings from a bank means that the bank must withdraw loans to others; to pay life insurance premiums with bonds means almost the same thing. Unless these and similar transactions cause the party at one end or the other to cut down his consumption in order to replace amounts thus withdrawn, no service has been done the national cause. To thus economize is just what the man who uses bonds to pay life insurance premiums or other obligations is not likely to do. It is because he doesn't want to make the extra sacrifice that he wants the privilege of using bonds as money. Of course, to borrow from a commercial bank to buy bonds is one of the quickest methods of causing inflation. The same result happens if the bank itself

buys bonds. With 4 per cent interest on government bonds, and even higher rates probable if the war continues much longer, there will be a terrible strain upon savings banks. The recent bond issue is causing a large withdrawal of savings deposits and banks themselves are subscribing to the bonds to prevent even greater withdrawals. As time goes on this is apt to become worse instead of better and with it inflation will grow apace.

If the reduction of consumption by two-fifths or a third of what we have been used to could be quickly brought about voluntarily or by a proper system of taxation, we could finance the war, that is, secure the men and commodities with which to prosecute it, without any process of inflation. But when these commodities and services cannot be gotten by voluntary saving and when there is too much objection to adequate taxation, then the government must resort to borrowing. If this is done upon a large scale, as in the present war, the banks are gradually forced to lend directly or indirectly and also to buy bonds themselves, in order that bond issues may not fail and that the government can get what it needs. Mr. Schiff³ openly advocates this increase of credit by the pyramiding of deposits, because, as he states, the people cannot or will not save enough.

But the heaviest taxes that are likely to be adopted will not prevent the consumption of many luxuries and near luxuries. Let us take one example. Even though it does have an effect, the present tax of 3 per cent, or even a tax of 25 per cent, on pleasure cars will not prevent many from being bought, although reduced incomes will have more effect. All unnecessary demand for such luxuries keeps from the army needed men and munitions. Why should not the government decide as in the case of coal, sugar and other commodities, who has a legitimate need for automobiles in war times and absolutely prohibit others from buying them? Many other similar examples suggest themselves to everyone. We might well go much further than we have in this direction; ordinary economic forces usually work fairly well in the long run, but they are too slow in many cases in an emergency like the present. Of course we would not disregard entirely the cautions given by Prof. H. C. Adams.⁴

Inasmuch as the problems of proper taxation are discussed

³See page 49.

⁴See page 28.

more at length elsewhere, we shall not go into details here, but we will call attention to the many cries that heavy taxation will hurt business, dry up the source of revenue and even cut down production at the time when it is most needed. This is a very serious matter in some of its aspects, and much care should be taken in levying proper taxation. Our present excess profits tax is far from perfect and has many wrinkles which need ironing out. But most of those who criticize heavy taxes upon business do so almost indiscriminately. It is unfortunate to hurt any business man or employe, but it is for the national good, in fact, absolutely essential, that unnecessary production should cease and that those engaged in such should go into the military service, or furnish supplies for the military, or do the work of others that the latter may help the government. The adjustment is painful and it should be handled with discretion but it should be forced. Those industries which minister to war needs will have such greatly increased demands that there is little danger that they will be taxed to death. Of course, such taxation is theoretically possible, but taxation which leaves 10 per cent or more net profit should not discourage the investment of capital in these lines nor the largest possible output, if the entrepreneurs of America have the least spark of unselfish patriotism. It would be all the more desirable to invest in these industries if others less useful were taxed more heavily. Existing tax measures intend to leave most of our war industries a much larger net profit than 10 per cent, though it is true that many difficulties, and particularly the matter of obsolescence, must be worked out.

We would not deny the function of credit which Professor Seligman⁵ emphasizes so much, in fact, we have already illustrated its advantages under certain conditions, but we think he lays too much stress upon subjective as opposed to objective costs. Where what is borrowed is destroyed as in this war, we think it important that people realize what are the objective costs, and that such a realization will have an effect upon subjective costs. If people are ignorant the immediate subjective costs of indirect taxation may be less than half that amount of direct taxation. But if they appreciate the facts, the subjective costs of the two taxes will be reversed and society will be better off for the change. Bond issues which cause inflation really amount to unduly heavy indirect taxes upon

⁵ See page 58 *ff.*

the masses, not in accordance with their ability to pay, but in proportion to their expenditures. It is important that both financiers and the masses realize this fact so that subjective costs shall harmonize with the public welfare.

In concluding let me give two homely illustrations of the main points which I have been trying to emphasize. The United States is so large that we cannot see it as a unit, hence let us consider a ranch or a plantation which is more or less isolated and self-sufficient. The father and his sons, perhaps the families of several sons, besides many helpers, are actively engaged in producing a living for the group. After the necessities are provided for, some can devote themselves to producing comforts and even luxuries. Suppose the neighboring ranches or plantations are beset by a powerful enemy and this ranch goes to their rescue. Would anybody argue that they can put off any of the war burdens till the future? Or would anybody urge that those who were making candy or silk dresses or pleasure cars, or other unnecessary things, should continue as usual? Would not all energies be directed to the most direct war purposes, and would not everyone reduce his demand for luxuries, and even for ordinary necessities as much as possible?

To take the second illustration. Let us look at our national income of 1910 as 30,000,000,000 gallons of milk instead of that many dollars worth of commodities and services. Suppose an increase of five or ten billions up to 1917, due to actual increased production, and a still further increase to forty-five or fifty billions due to pouring in of water. Suppose at this time a war makes it necessary that the government have twenty billions of this total of fifty billions. The government may take different methods to secure this amount. It may get it by taxing or by borrowing. If these methods cause a corresponding reduction in consumption of milk, this can be accomplished successfully, but if one method, say borrowing, caused a dilution of the milk, difficulty arises. If such evasion of economy is attempted, the government is forced to pour in water or to have others pour in water for it. By pouring in thirty or thirty-five billions of gallons there is made a total of eighty or eighty-five billions. The government can then take out thirty or thirty-five billions and get twenty billions of real milk and the public can have left for civil needs fifty billion gallons of what it calls milk but which is really very much less. A reduction of consumption has thus been forced,

not by taxes but by inflation. Those who received a stated income still receive the same number of gallons (or dollars) or even possibly somewhat more, but the food value (or purchasing power) is much lessened.

These two illustrations bring home three important points: first, that the burden of the war cannot possibly be put off till the future; second, that the burden is enormous and inevitable and cannot be met by any financial makeshift, but demands unusual and stringent economy; and third, that attempts to shirk economy through excessive loans will not make the burden less but will distribute it much more inequitably.

As we have intimated above, the fundamental thing in our war finance is the stimulation of production for war which is possible only through reduction of consumption. This reduction is even more important practically than a total increased production, because it has much greater possibilities within a short time. If we will cease to delude ourselves about the possibility of shifting a large part of the immense burden upon the future, or of avoiding it in other impossible ways, and really recognize the task as it is and undertake to grapple with it, we can avoid some of the terrible mistakes of the past. This means that we should now raise larger amounts by taxation, and that an even greater proportion should be so raised hereafter as industry becomes more adjusted to the changed conditions. Furthermore, economies should be forced by governmental suspension of unnecessary production.

The present limit to taxation is psychological. That limit may well be pushed much further if there can be a general appreciation of the real ways in which the war may be financed. The danger is that in trying to escape the discomforts of the great economies which are absolutely necessary, we shall, through excessive borrowing, throw an increasing amount of the financing upon the banks. There is little likelihood that the government will use paper money; that has been too much discredited. While that method might have been resorted to in Civil War and previous times when note issue banking was common, in the present the much more subtle and effective method is through the pyramiding of deposits, as actually advocated by Mr. Schiff.⁶ By trying to escape thus, the nation shall not escape, but shall be forced to even greater sacrifices. In

⁶ See page 49.

fact, it shall force its masses, who can least afford to economize, to a greatly reduced consumption through a further decreased purchasing power of the money medium.

To thus secure the reduction necessary to win the war through inflation is most inequitable and probably the most disastrous method in the long run. "To make the world safe for democracy" is flaunted upon our banners. It is a worthy battle cry in our supreme struggle with Prussian autocracy. But in the adaptation of means to ends it should not be disregarded at home at the fountain head of democracy.